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ABSTRACT

This report evaluates the need for K-12 capital spending in Tennessee and the methods the state uses to meet this need within a national context. The report examines the benefits of capital outlay spending and its impact on student performance. It identifies the major drivers of capital expenses. The report then investigates the roles the federal government and other state governments play in funding these expenses and how Tennessee compares to other states. Finally, it identifies strengths and weaknesses of Tennessee's existing funding programs and suggests possible improvements. The report's conclusions include: (1) based on the condition of existing facilities, Tennessee's school construction needs are significant but less than those found in other states; (2) based on enrollment growth, Tennessee's school construction needs are comparable to those of the rest of the nation and will decline in the coming decade; (3) legal challenges have increased state capital funding in Tennessee, but not to the extent found in other states; and (4) total K-12 capital spending in Tennessee increased more rapidly over the past decade than did spending nationwide, but probably remains below the national average. (EV)

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School Capital Funding:

Tennessee in a National Context

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Richard Gurley
Associate Legislative Research Analyst

Ethel R. Detch, Director
Office of Education Accountability
505 Deaderick Street, Suite 1700
Nashville, TN 37243-0268
615/401-7911
www.comptroller.state.tn.us/orea/reports

John G. Morgan
Comptroller of the Treasury

August 2002

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STATE OF TENNESSEE

John G. Morgan
Comptroller

COMPTROLLER OF THE TREASURY

STATE CAPITOL
NASHVILLE, TENNESSEE 37243-0264
PHONE (615) 741-2501

August 16, 2002

The Honorable John S. Wilder
Speaker of the Senate
The Honorable Jimmy Naifeh
Speaker of the House of Representatives
And
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

Transmitted herewith is a report prepared by the Office of Education Accountability concerning K-12 capital finance in Tennessee. The report provides information and recommendations that may be useful to policymakers in considering ways to improve Tennessee's methods of financing school construction and renovation projects.

Sincerely,

John G. Morgan
Comptroller of the Treasury

Executive Summary

School buildings are perhaps the most visible expression of society's investment in K-12 education. Quality facilities can increase teacher satisfaction, allow for the incorporation of new technology into the classroom, and lower utility costs through improved energy efficiency. Most importantly, research has shown that inadequate facilities can lower student performance.

In the past, states generally considered construction and renovation projects to be local responsibilities.[1] The primary method local school districts use to finance capital projects is general obligation bonds backed by local property tax revenue. This heavy reliance on local property taxes has often produced inequity in school facilities among districts and has also led to concern (and lawsuits) about the adequacy of school facilities in poorer districts.[2] The entrance of the baby boom echo into public schools in the 1980s and 1990s exacerbated these problems.[3] As a result, many states have taken a more active role in K-12 capital finance over the past decade. Increasing state involvement in capital spending has taken a number of forms, including:

- Credit enhancement programs
- Loan programs
- Nonrecurring funding (usually bond initiatives)
- Annual funding programs
- State oversight mechanisms

This report evaluates the need for K-12 capital spending in Tennessee and the methods the state uses to meet this need within a national context. The report examines the benefits of capital outlay spending and its impact on student performance. It identifies the major drivers of capital expenses. The report then investigates the roles the federal government and other state governments play in funding these expenses and how Tennessee compares to other states. Finally, it identifies strengths and weaknesses of Tennessee's existing funding programs and suggests possible improvements. This report concludes:

Based on the condition of existing facilities, Tennessee's school construction needs are significant but less than those found in other states. In March 2002, the Tennessee Advisory Commission on Intergovernmental Relations (TACIR) published a study entitled *Building Tennessee's Tomorrow: A Survey of Infrastructure Needs Inventory.* According to survey responses, school districts face approximately $4.8 billion in capital needs from July 2001 through June 2006.[4] In the 1996 U.S. General Accounting Office (GAO) study, *School Facilities: America's Schools Report Differing Conditions*, 74.7

[1] Jessica Sandham, "Capitol Expenditures," *Education Week*, June 20, 2001.
[2] Eric J. Brunner and Kim Rueben, "Financing New School Construction and Modernization: Evidence from California," *National Tax Journal*, September 2001, p. 527.
[3] The baby boom echo generation includes births from the late 1970s through the early 1990s. This demographic group is much larger than "Generation X" which preceded it and "The Millennials" which will follow it.
[4] Tennessee Advisory Commission on Intergovernmental Relations, *Building Tennessee's Tomorrow: Anticipating the State's Infrastructure Needs*, March 2002, p. 11.

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percent of Tennessee's K-12 schools required some improvement to bring them into good overall condition. While that number seems high, only four states had a lower percentage of schools requiring improvements.[5] In Tennessee, only 12.5 percent of schools required more than $1.7 million in improvements to reach good condition; thirty-nine states had a higher percentage.[6] (See page 24.)

Based on enrollment growth, Tennessee's school construction needs are comparable to those of the rest of the nation and will decline in the coming decade. Tennessee public school enrollment grew 9.8 from 1991 to 2000. The National Center for Education Statistics (NCES) predicts enrollment growth to decline to 1.7 percent from 2000 to 2009.[7] Both these numbers are close to the national average. Growth rates for individual districts vary considerably. From 1992 to 2001 average daily membership declined by 34 percent (3.0 percent annually) in Fayette County while ADM increased by 62 percent (5.5 percent annually) in Williamson County over the same period.[8] (See page 24.)

Legal challenges have increased state capital funding in Tennessee, but not to the extent found in other states. In anticipation of the Tennessee Supreme Court's 1993 *Small Schools v. McWherter* decision, the General Assembly implemented the BEP through the 1992 Education Improvement Act to address these issues. Plaintiffs challenged the adequacy of some aspects of BEP funding, including capital outlay, in *Small Schools v. McWherter II*. However, the court ruled in favor of the state on the issue of capital, and the original school construction component of the BEP has remained intact. Many states have not adjusted their capital funding programs in response to legal challenges while others have implemented much more expansive solutions than the BEP. (See page 25.)

According to TACIR's infrastructure report, Tennessee school districts must construct new facilities to remain in compliance with EIA class size mandates. The Education Improvement Act (EIA) passed by the General Assembly in 1992 established strict limits on class size throughout the state.[9] TACIR's infrastructure report cited a cost of $1.35 billion for construction of new classrooms from July 2001 to June 2006 in order to house classes mandated by the EIA.[10] TACIR based this conclusion on student/teacher ratios for the 1991-92 and 2001-02 school years, mandates in the EIA, and enrollment growth patterns. (See page 25.)

Total K-12 capital spending in Tennessee increased more rapidly over the past decade than did spending nationwide, but probably remains below the national average. In constant 1997 dollars, total public K-12 capital spending[11] in Tennessee grew 104.5 percent in only seven years even after adjusting for inflation, compared to 39

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[5] Hawaii, Montana, Pennsylvania and Georgia.
[6] US General Accounting Office, "School Facilities: America's Schools Report Differing Conditions," June 1996.
[7] National Center for Education Statistics, *Projections of Education Statistics to 2009*, July 1999, Table 4, and *Projections of Education Statistics to 2011*, August 2001, Table 4.
[8] Office of Education Accountability, internal review and analysis of school system data.
[9] TCA §49-1-104.
[10] Tennessee Advisory Commission on Intergovernmental Relations, *Building Tennessee's Tomorrow: Anticipating the State's Infrastructure Needs*, March 2002, p. 29.
[11] Local capital spending including local revenue, state funding, and national funding.

percent nationwide.[12] Average daily membership (ADM) grew 8.2 percent during this time. Inflation-adjusted spending per ADM increased 89 percent from 1990 to1997, reaching $426.[13] While capital spending in Tennessee rose much more rapidly in the 1990s than in the nation as a whole, in 1997 it remained approximately 20 percent below the national average of $535 per pupil.[14] This discrepancy is probably partially due to lower construction costs.

Recent national data that correlates to the 1997 GAO report is unavailable. However, school district spending on capital projects in Tennessee has continued to grow rapidly. According to the Tennessee Department of Education Annual Financial Reports, K-12 capital spending, when adjusted for inflation,[15] increased by 47 percent from fiscal year 1997 to fiscal year 2000.[16] (See page 26.)

Tennessee lacks consistent and clear data on district-level capital projects and spending. The Department of Education and the Comptroller's Division of Local Finance both have substantial financial data on capital spending and bonded debt. However, this data is difficult to analyze. The Department's Annual Financial Reports contain budget codes for capital spending but do not show the number, cost, and type of individual projects. The Division of Local Finance maintains records of bond issues for K-12 capital projects within a larger database of local government debt. In order to isolate school district debt, these bond issuances must be pulled from the database manually. (See page 27.)

Though Tennessee spends below the national average for K-12 construction and renovation projects, the state spending for capital outlay is high relative to other state programs. Based on information collected from state education agencies, Tennessee spent $189 per student on K-12 capital projects in fiscal year 2001. Though this is 77 percent of the national average, because Tennessee is a low-spending state, K-12 capital outlay receives *more* funding relative to other programs while still being funded at lower levels than other states. In fiscal year 2001, Tennessee spent an estimated $3,328 state dollars per pupil on K-12 education. This amount is 68 percent of the national average.[17] The state tax burden in Tennessee for the year 2000 was $1,360 per capita. This is only 71 percent of the national average of $1,921 per capita,[18] indicating that Tennessee spends relatively more on K-12 capital outlay than it does on government services taken as a whole. (See page 27.)

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[12] US General Accounting Office, "School Facilities: Construction Expenditures Have Grown Significantly in Recent Years," March 2000, p. 27.

[13] Tennessee Department of Education, *Annual Statistical Report for the Scholastic Year ending June 30, 1990*, Table 7A and *Annual Statistical Report for the Scholastic Year ending June 30, 1997*, Table 7A.

[14] Based on NCES enrollment data. National Center for Education Statistics, *Projections of Education Statistics to 2011*, August 2001, p. 27.

[15] Using Engineering News Record "Construction Cost Index," http://www.enr.com/cost/costcci.asp (accessed November 9, 2001).

[16] Tennessee Department of Education, *Annual Financial Report for the Scholastic Year ending June 30, 1997* and *Annual Financial Report for the Scholastic Year ending June 30, 2000*, Budget Codes 76100000 and 91300000.

[17] "Estimated Fiscal 2001 Elementary and Secondary Education Expenditures," National Association of State Budget Officers, *2000 State Expenditure Report*, June 2001, p. 17; National Center for Education Statistics, *Projections of Education Statistics to 2011*, August 2001, Table 4.

[18] Federation of Tax Administrators, "2000 State Tax Revenue," http://www.taxadmin.org/fta/rate/00taxbur.html (accessed November 7, 2001).

Tennessee's methods of BEP funding provide districts with high levels of local control. Tennessee does not require local districts to submit long-range facilities plans to the state. It also does not require state approval for capital projects using state BEP funding. Thus, school district officials are free to meet local needs in the manner they believe most effective without altering their projects or goals to meet state standards.

Tennessee also allows districts to use BEP-generated dollars for many purposes. Though the state allocates a certain portion for capital outlay, districts may use these funds to meet other needs. Also, certain other BEP components may be used for capital projects, and districts are free to spend more or less than their local portion of BEP school construction funding would indicate. These features give local districts significant latitude with which to allocate state resources. Because of this emphasis on local control, the department does not maintain staff dedicated to capital outlay. (See page 28.)

Tennessee's funding of capital outlay through the BEP has a number of strengths. BEP funding provides a stable revenue source. The fiscal capacity index directs a greater share of state funding to those districts with more limited local revenue sources. Because districts ultimately bear the costs of improvements upon current programs, the BEP provides implicit incentives for cost-effectiveness and does not allow districts to increase their level of state funding artificially. (See page 28.)

Tennessee's BEP funding also has several weaknesses. Districts with rapid enrollment growth often have greater capital spending needs. These needs are not addressed by the BEP. School districts may face capital needs above the BEP and have difficulty raising local revenues to meet these needs. Finally, the BEP does not include a mechanism to lower borrowing costs. Most local governments purchase credit enhancement in the private sector when issuing bonds for school construction. (See page 29.)

Legislative Recommendations

- **The General Assembly may wish to consider implementing a credit enhancement program to lower finance costs facing local school districts.**
- **The General Assembly may wish to increase BEP capital outlay funding within the context of increases in overall BEP spending.**
- **The General Assembly may wish to consider an additional factor within the BEP capital outlay component to account for rapid enrollment growth.**

Department of Education Comments

In response to a draft of this report, the Commissioner of Education offered these comments:

LEAs in Tennessee have been utilizing BEP funding to renovate and construct school facilities since the formula was implemented in 1992. Under the previous funding formula, capital outlay funding had to be used for this purpose, but the total state capital outlay funds were an inadequate $13 million. Therefore, almost all renovation and construction costs were paid with local dollars. As an example of the increase in state funding available for capital outlay projects, the 2002-03 fiscal year capital outlay

component generated by the BEP totals $381,857,824. Since capital outlay is a nonclassroom component, the state funds, on average, 50 percent of the dollars generated in the formula.

The fiscal needs of rapidly growing LEAs are not necessarily capital outlay in nature. A LEA with a rapidly growing enrollment might have the building space to accommodate more students, but need additional teachers and instructional supplies.

BEP funding is always calculated on average daily membership from the prior school year. Growth funding is provided from a separate allocation of money provided by the General Assembly. Based on recent changes in statute, the growth threshold is not always two percent. The law now grants the Department of Education flexibility to adjust the threshold so that all money appropriated by the General Assembly for growth can be distributed to LEAs. The BEP is recalculated for rapidly growing systems based on their increase in average daily membership. As a result, the capital outlay component, as well as other components in the BEP, are recalculated and additional funds are provided to these systems.

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Introduction

School buildings are perhaps the most visible expression of society's investment in K-12 education. The publication of Jonathan Kozol's *Savage Inequalities* in 1991 produced a public outcry over the poor conditions of many of our nation's school facilities.[1] In the mid-1990s the U.S. General Accounting Office (GAO) released four separate reports on the condition of America's school facilities. The U.S. Department of Education followed up with its own study in 1999, and *Education Week* published a special report on facilities needs and state efforts to address those needs in June 2001. These reports and others have increased attention to K-12 capital needs in recent years.

Capital outlays are expenditures on construction and renovation projects. Traditionally local school districts have borne most of the financial burden for K-12 capital outlay. Over the past decade many states have taken a more active role in helping local districts finance capital projects in response to rapid enrollment growth and the deterioration of older facilities; others have maintained that capital outlay is primarily a local responsibility. This report examines the need for K-12 capital spending in Tennessee and the methods the state uses to meet this need within a national context. Specifically the report answers the following questions:

- What are the benefits of capital outlay spending and what is its impact on student performance?
- What drives capital expenses?
- What roles do state governments and the federal government take in funding these expenses?
- How does Tennessee compare to other states?
- What are the strengths and weaknesses of Tennessee's funding programs, and what improvements could be made?

Methodology

The conclusions reached and recommendations made in this report are based on the following:

- Interviews with contractors who have built schools in Tennessee and surrounding states.
- An extensive review of research literature concerning K-12 capital issues.
- A review of data on enrollment growth, facilities conditions, and capital spending for Tennessee and other states.
- A review of Tennessee's capital funding methods within the BEP.

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[1] Jonathan Kozol, *Savage Inequalities*, (New York: Harper Perennial, 1992).

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- The Office of Education Accountability (OEA) State School Construction Aid Survey, a survey of the K-12 capital finance programs of all 50 states.

Data collection for the State School Construction Aid Survey was essentially a three-step process. First, OEA developed a contact list of K-12 education capital finance specialists in each state. On July 30, 2001, each state representative was sent a copy of the State School Construction Aid Survey to complete and return to the office. (See Appendix A.) Upon receipt of a state's survey, the office constructed a state profile using information contained therein, information from state web sites, and additional outside sources. (See Appendix B.) Finally, the office sent each state's profile to that state's respondent and asked the respondent to correct or verify information contained in the profile. In several cases, the respondent was also asked to elaborate on one or more aspects of state programs.

Forty-five of the 50 states completed and returned surveys sent from this office. Of those states, 37 subsequently reviewed, edited, and verified their state profiles. Profiles for Alabama, Arizona, Colorado, Louisiana, Michigan, Minnesota, Montana, and Oklahoma did not receive final verification. Five states (New York, Oregon, Virginia, Washington, and Wisconsin) did not complete surveys. Profiles for these states were constructed using only outside sources. Each of these states subsequently reviewed, edited, and confirmed information in their state profile. Thus, all profiles represent some level of direct state input.

Background

Benefits of Capital Spending

Capital projects are obviously necessary—very little learning could take place without school buildings to house students and teachers. Research links capital spending to specific benefits, including increased student performance, teacher satisfaction, and energy efficiency. Capital projects also generally enhance a school's ability to incorporate new technology.

Facilities Condition and Student Performance

Quality school facilities are one component of a positive learning environment. Numerous studies suggest that students perform better in better facilities.[2] However, this research presents several problems. The most pressing of these is separating building conditions from other factors that could potentially affect student outcomes. For example, common sense states that strong administrative leadership will often lead to better maintenance of existing facilities. In these cases, saying that better facilities produced

[2] Glen Earthman, "Review of Research on the Relationship between School Buildings, Student Achievement, and Student Behavior," Virginia Polytechnic Institute and State University, July 1996, p. 22; Glen Earthman, "The Impact of School Building Condition and Student Achievement, and Behavior," Virginia Polytechnic Institute and State University, July 1996; J. Howard Bowers and Charles Burkett, "Physical Environment Influences Related to Student Achievement, Health, Attendance and Behavior," *CEFP Journal*, July/August 1988, p.33-34; Eric Hines, *Building Condition and Student Achievement*, Virginia Polytechnic Institute and State University, July 1996; Glen Earthman, Carol Cash, and Denny Van Berkum, "Student Achievement and Behavior and School Building Age," *The Journal of School Business Management*, vol. 8, no. 3, 1995, p. 27-37.

higher test scores might be incorrect—the test scores and facilities conditions are both a result of stronger administration. Similarly, high levels of parental and community involvement can promote both good facility conditions and student achievement. In both of these examples, the factors influencing higher test scores are not the facilities' conditions themselves but the underlying cause of those facilities' conditions. Districts that spend more on capital and maintenance are also likely to spend more in other areas. Thus, when students in quality facilities perform well, their performance may be attributable to higher quality teachers or more classroom supplies, not the facilities. These concerns limit the conclusions that can be drawn from much of the existing research on facility conditions and student achievement. Still, research suggests some connection between quality facilities and higher academic performance.

Teacher Satisfaction

Some researchers theorize that the condition of school facilities can influence teacher satisfaction. OEA staff found no rigorous statistical work that examines this relationship. However, some research has suggested that environmental conditions can influence teacher self-esteem and sense of worth.[3]

Energy Efficiency

In addition to contributing to a lower quality education for students, poor school facilities can also increase costs to local districts. In 1994, the U.S. General Accounting Office (GAO) found that 41 percent of schools had poor energy efficiency because of substandard building conditions.[4] Taxpayers must pay for higher heating, cooling, and electric bills for these schools.

New Technology

New technologies have evolved rapidly in recent years. Multimedia and broadband technology are now considered necessary for a quality education. These technologies require substantial infrastructure as well as individual computers. In 1999, the Southern Regional Education Board concluded that school districts should install local area networks (LANs) and that "all administrative and classroom computers should be connected to the LAN"[5] Many older buildings lack not only LAN connections but also sufficient electrical wiring to accommodate new technology. A 1995 GAO study stated, "Although designing a new building with this [technology] infrastructure included is relatively easy and inexpensive, installing it in existing school buildings can be expensive and disruptive."[6]

Drivers of Capital Spending Needs

Public school capital needs in the United States have increased considerably in recent years. Two primary factors drive capital spending needs: deteriorating facilities and

[3] Glen Earthman, "Review of Research on the Relationship between School Buildings, Student Achievement, and Student Behavior," Virginia Polytechnic Institute and State University, July 1996, p. 16.
[4] US General Accounting Office, *School Facilities: Conditions of America's Schools*, June 1996, pp. 10-11.
[5] Lou Parker and William Thomas, Southern Regional Education Board, *Guidelines for Technology Equipment Selection and Use: An SREB Model for Schools and Campuses*, June 1999, pp. 4-5.
[6] US General Accounting Office, *School Facilities: America's Schools not Designed or Equipped for 21st Century*, April 1995, letter 2.2.1.

enrollment growth. Many of the nation's school facilities were built in the 1950s, when the baby boom generation entered school. These buildings are nearing the end of their useful life. Simultaneously, school enrollments have swelled in recent years. State courts also have driven increased capital funding in states where the courts determined finance methods were either inadequate or inequitable. These factors have led to unprecedented levels of K-12 capital spending in recent years. A 2000 GAO study found that school construction expenditures nationally grew 39 percent from fiscal year 1990 to fiscal year 1997, even after adjusting for inflation.[7] Finally, some spending increases in recent years reflect higher public expectations for more classrooms to accommodate smaller class sizes, higher quality facilities, and more advanced technology.

Deteriorating Facilities

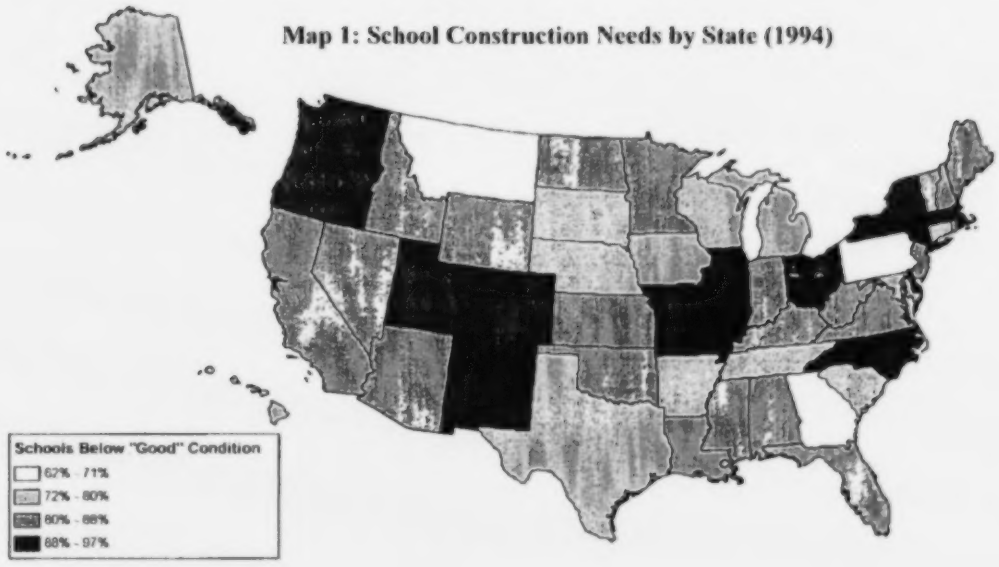
Schools, like all buildings, have a limited life span. As stated earlier, districts may have difficulty incorporating new technology into older buildings. Districts may also develop new needs that existing facilities are unequipped to meet. And, as buildings age districts must spend increasing amounts of money simply to maintain schools in an adequate state. Eventually, even well-maintained buildings must be replaced. Thus, the condition and age of facilities exerts significant influence on capital spending needs.

The most reliable state-level data available on school facilities' conditions is a 1996 U.S. General Accounting Office study, *School Facilities: America's Schools Report Differing Conditions*. In 1994, the GAO surveyed a representative sample of rural, urban, and suburban schools in every state. The study examined factors such as the condition of roofs, framing, floors, foundations, walls, windows, doors, finishes, and plumbing; general condition of HVAC (heating, ventilation and air conditioning) and electrical systems and compliance with safety codes; and environmental conditions including lighting, heating, ventilation, indoor air quality, acoustics for noise control, flexibility of instructional space, and physical security of buildings. The GAO found that 84 percent of schools required additional funding to bring their facilities up to "good" condition. The average funding need for these schools was $1.7 million. Schools with needs greater than $1.7 million were determined to have major funding needs. The study also provides state-level data on school conditions and the percent of schools with funding needs (See Maps 1 and 2.)[8]

[7] US General Accounting Office, *School Facilities: Construction Expenditures Have Grown Significantly in Recent Years*, March 2000, p. 27.

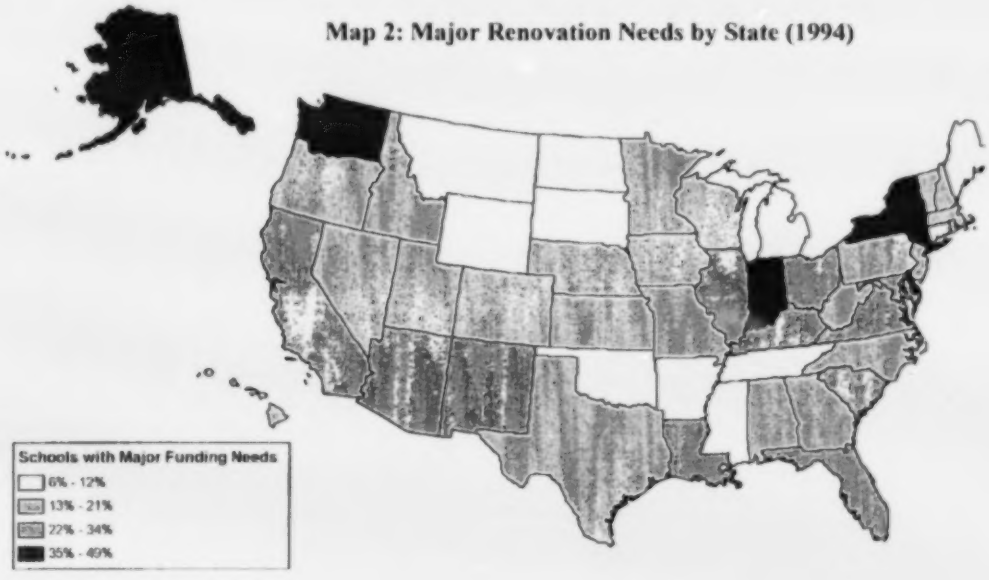
[8] US General Accounting Office, *School Facilities: America's Schools Report Differing Conditions*, June 1996, p. 67.

Map 1: School Construction Needs by State (1994)



Source: US General Accounting Office, *School Facilities: America's Schools Report Differing Conditions*, June 1996, p. 67.

Map 2: Major Renovation Needs by State (1994)



Source: US General Accounting Office, *School Facilities: America's Schools Report Differing Conditions*, June 1996, p. 67.

Because the GAO study was based on survey data, it did not provide estimates of the total need for repair and replacement of schools in each state. However, it estimated the cost of bringing all public school buildings nationwide into "good" condition was $112 billion.[9] This amount includes $11 billion necessary to meet federal mandates, including asbestos removal and accessibility for disabled students.[10]

In 1999, five years after the GAO survey, the U.S. Department of Education National Center for Education Statistics (NCES) conducted a study of school conditions using similar methodology as the GAO study. The NCES research found that from 1994 to 1999, the number of schools requiring repairs or renovations to bring them into "good" condition had fallen from 84 percent to 76 percent. However, the average dollar amount needed to bring schools to "good" overall condition had grown $2.2 million,[11] and the total cost had risen to approximately $127 billion.[12] This translates to an average cost of $3,800 per student in those schools needing repairs or $2,900 per student when schools not needing repairs are included.[13]

Enrollment Growth

If future enrollment is expected to grow beyond current levels, new schools will be necessary. During the 1980s and 1990s, K-12 enrollment swelled as the "baby boom echo" generation entered school. The U.S. population under 18 has now stabilized. Thus, public school enrollment growth nationwide is expected to slow from 10.6 percent from 1991 to 2000 to 0.3 percent from 2000 to 2009 according to projections from the National Center for Education Statistics (NCES).[14] However, enrollment changes in individual states vary considerably: Western states should continue to experience substantial enrollment growth as the Upper Midwest and New England see significant declines in enrollment. (See Maps 3 and 4.)

Lawsuits/Court Decisions

Seventeen states have revised their funding methods for capital outlay and debt service in response to lawsuits. (See Map 5.) Most suits challenged the adequacy and/or equity of the state's education finance mechanisms as a whole. This total of 17 includes all states that altered their capital finance programs as a result of a lawsuit, regardless of whether or not capital finance was the primary issue in the suit. It also includes suits that drove changes in capital finance methods even if the courts ruled in favor of the state. In some cases, state legislatures passed new initiatives as suits made their way through the judicial system. In these cases, the policies that motivated some suits had been rescinded by the time state courts ruled, but the suit was an impetus for change at the state level.

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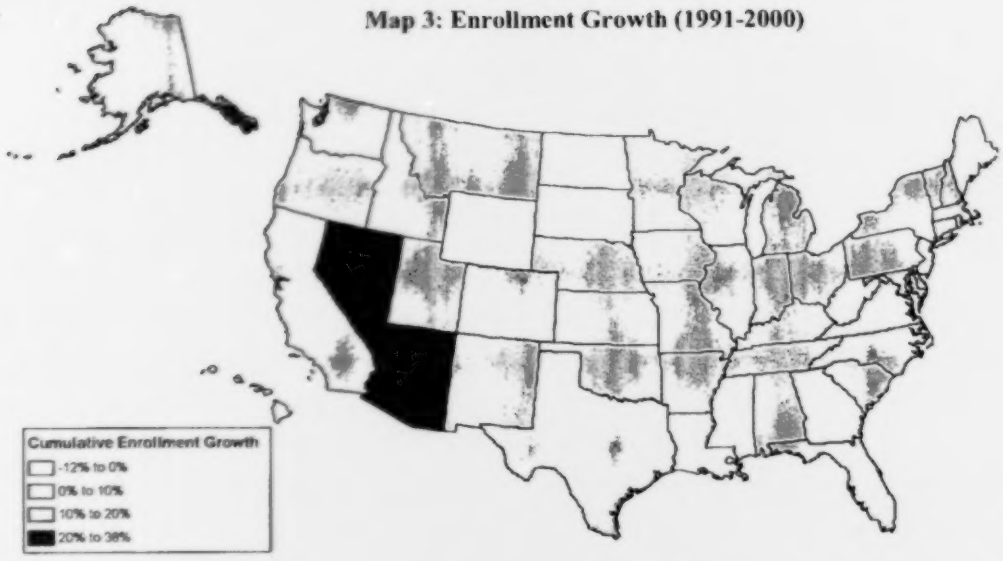
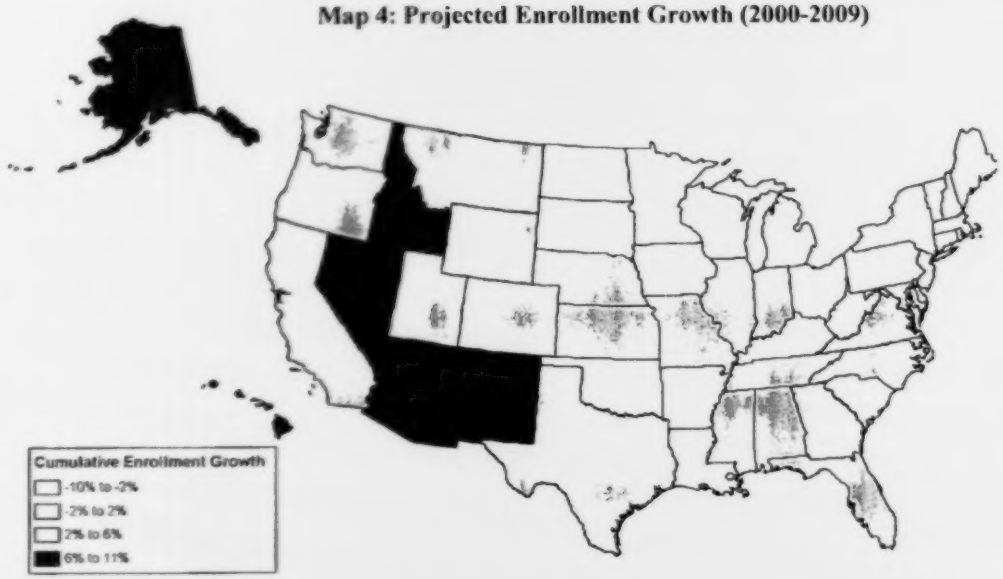
[9] US General Accounting Office, *School Facilities: America's Schools Report Differing Conditions*, June 1996, p. 12.
[10] Bernie Greer, project officer, *Condition of America's Public School Facilities: 1999*, (Washington, DC: National Center for Education Statistics, 2000), p. 2.
[11] Ibid., pp. 15-16.
[12] Ibid., Appendix B, Table 23.
[13] Ibid., pp. 17.
[14] National Center for Education Statistics, *Projections of Education Statistics to 2009*, July 1999, Table 45 and National Center for Education Statistics, *Projections of Education Statistics to 2011*, August 2001, Table 4.

Map 3: Enrollment Growth (1991-2000)



Map 4: Projected Enrollment Growth (2000-2009)



Sources: National Center for Education Statistics, *Projections of Education Statistics to 2009*, July 1999, Table 45 and National Center for Education Statistics, *Projections of Education Statistics to 2011*, August 2001, Table 4.

As of September 2001, nine states were facing court challenges to their methods of financing capital outlay. This includes five states that have already altered their state capital funding programs as a result of legal action.

Map 5: State Capital Finance Lawsuits (2001)

Source: OEA, State School Construction Aid Survey

State Roles in K-12 Capital Outlay and Debt Service

In the past, states generally considered construction and renovation projects to be local responsibilities.[15] Local school districts primarily use general obligation bonds backed by local property tax revenue to finance capital projects. This heavy reliance on local property taxes has often produced inequity in school facilities among districts and has also led to concern (and lawsuits) about the adequacy of school facilities in poorer districts.[16] The entrance of the baby boom echo into public schools in the 1980s and 1990s exacerbated these problems. As a result, many states have taken a more active role in K-12 capital finance over the past decade. Increasing state involvement in capital spending has taken a number of forms. These are:

- Credit enhancement programs
- Loan programs
- Nonrecurring funding (usually bond initiatives)
- Annual funding programs

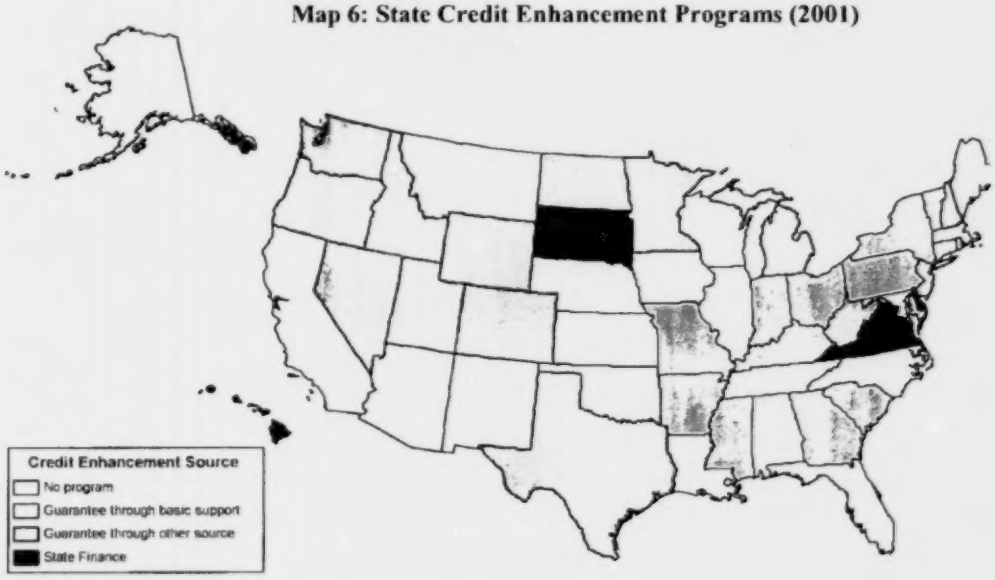
[15] Jessica Sandham, "Capitol Expenditures," *Education Week*, June 20, 2001.
[16] Eric J. Brunner and Kim Rueben, "Financing New School Construction and Modernization: Evidence from California," *National Tax Journal*, September 2001, p. 527.

- State oversight mechanisms

State Credit Enhancement Programs

Credit enhancement programs allow states to reduce the borrowing costs of local school districts, often at minimal cost to the state. Twenty-nine states currently have some type of credit enhancement program in place. (See Map 6.)

Map 6: State Credit Enhancement Programs (2001)



Source: OEA, State School Construction Aid Survey

The most common form of credit enhancement is a state guarantee of local general obligation bonds. When school districts float bond issues they contract with a local paying agent to handle the mechanics of payments. As bonds reach maturity, the districts forward to the paying agent funds necessary to meet current debt service obligations. The paying agent then uses this money to pay bondholders. In states with credit enhancement programs, the paying agent notifies the state if the local government appears unable to meet its obligation. Most state guarantee programs are designed to ensure that bondholders can receive the principal and interest on their bonds on the day of maturity. Thus, the paying agent will notify the state approximately 10 business days prior to bond maturity if the local district does not appear to have sufficient funds on hand to meet its debt service obligations. The state then forwards state funds to the paying agent. The mechanics of individual programs differ somewhat, but most fit this general description.

Aid Intercept Guarantee Programs

With the exception of Hawaii,[17] all states have a basic support program to fund public education. These support programs consist of state payments to local districts.

[17] Hawaii finances all elementary and secondary education needs at the state level.

Tennessee's basic support program is the Basic Education Program (BEP). Elevenstates guarantee local bonds through theseannual state aid payments. (See Map 6.) That is, if a local district defaults on its bonded debt, the state steps in and uses basic support funding due the district to pay bondholders. This is the simplest form of guarantee in that it does not require the state to create an additional revenue stream or fund to provide backing for bonds.

Missouri's School District Direct Deposit Program diverts monthly state aid directly to a bank serving as a trustee. Districts use local revenue that would have gone to payoff the bond issue to replace the state aid. The Direct Deposit Program reimburses districts for the cost of bond issuance (up to twopercent of bond value) using revenue derived from riverboat gambling.

In 1998, Mississippi allowed districts to use future state Mississippi Adequate Education Program (MAEP) funding to guarantee local bonds for capital needs. That was a onetime opportunity that has since been discontinued, but many Mississippi districts currently have outstanding bonds guaranteed by MAEP funds.

Other Guarantee Programs

Although basic support funding amounts to several thousand dollars per student for most states, it is often insufficient to provide optimal credit enhancement for local districts. Thus, four states (Colorado, Nevada, New Jersey, and Utah) use other sources in addition to annual state aid to back district bonds. Ten other states have bond guarantee programs that draw from sources other than annual state aid (See Map 6.) Six of these states use some type of permanent fund as the source of the guarantee.[18] Idaho and Washington both provide a backup general obligation pledge to cover guaranteed bonds. Minnesota and West Virginia appropriate funds on an annual basis to cover any local defaults on guaranteed bonds. Some of these states have explicit statutory provisions to ensure the districts repay the state with interest. Some also allow the state to charge the district an additional penalty for a default. Oregon's program authorizes the state to reimburse itself from various state payments that would be due a defaulting district.

New Jersey is unique in that it has multiple bond guarantee programs, one using annual state aid payments and two using additional resources beyond these payments. In 2000, Moody's Investor Services gave New Jersey's State Qualified Bond Program (bonds guaranteed by annual state aid) an "A" rating.[19] In contrast, its Additional State Aid Bonds Program and its New Jersey Fund for the Support of Free Public Schools Program both received "AA" ratings, a reflection of the decreased risk associated with broadening the guarantee base. Bond programs succeed by convincing investors that the credit enhancement program reduces the risk of local bonds. Perceptions that the program substantially decreases risk will result in a higher rating, which in turn will lower the finance costs incurred by local school districts.

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[18] Michigan, New Hampshire, Oklahoma, Oregon, Texas, and Wyoming

[19] Under Moody's rating methodology, a rating of AA is higher than a rating of A. AAA is the highest rating. Higher ratings reflect decreased risks and sounder investments.

West Virginia requires all debt service payments on locally-issued general obligation bonds (including school bonds) to beremitted to the state Municipal Bond Commission. The commission takes the place of a traditional paying agent, and the state legislature makes an annual blanket appropriation authorizing the governor to meet any deficiency in the state sinking fund as a result of a district failure to meet debt service obligations.

State Bond Programs

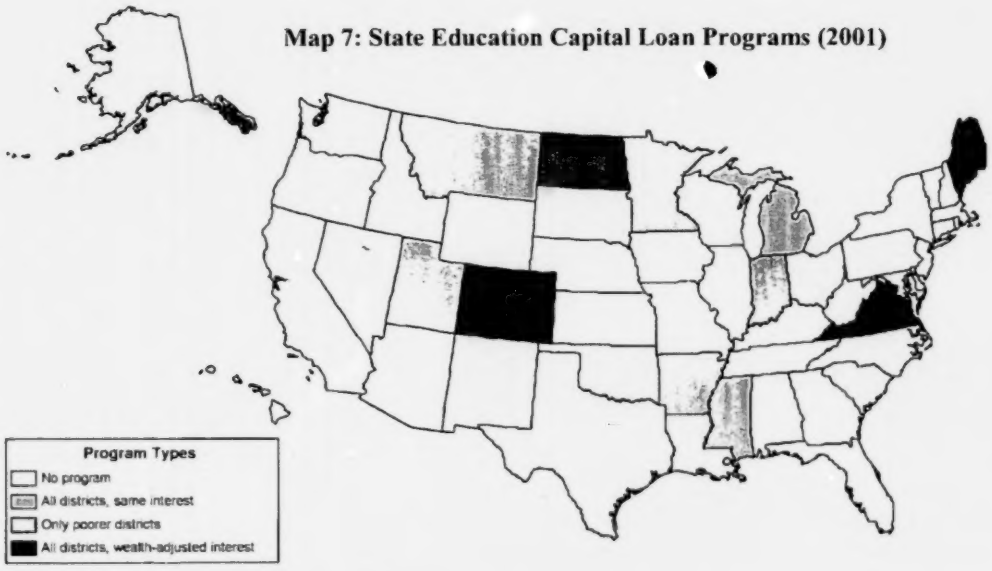
Three states, Delaware, South Dakota, and Virginia, finance capital construction through state bonds. Delaware issues bonds in the name of the district when local voters approve a bond referendum and the state education agency determines the district needs additional school facilities. South Dakota requires local districts to enter into lease purchase agreements with the state. Virginia, like Delaware, issues bonds in the name of the local government. Virginia intercepts state aid due the district in the event of a default.

As states assume some of the risk borne by bondholders under these programs, several have taken steps to minimize that risk. Many states with bond guarantee programs require districts to meet certain financial standards before the state will guarantee local bonds. Though some of these standards are more exacting than others, all are intended to protect the state from guaranteeing the debt obligations of districts that are not financially sound. Colorado's program mandates that the state conduct an audit of any district that defaults on guaranteed debt. While these features decrease the risk borne by the state, it is important to note that the risk is relatively small. Most state officials contacted expressed great confidence in the financial solvency of local districts and a number of states have never had a local school district fail to meet its debt service obligations.

State Loan Programs

Although local general obligation bonds are usually the primary means school districts use to finance capital outlay, 10 states allow local districts to borrow from the state for capital projects. (See Map 7.) These loans usually come from a fund set aside for the purpose of district capital loans. Most states limit the amount any individual district may borrow at one time, often by statute. Minnesota and Indiana offer loansonly to low-wealth districts. Colorado, North Dakota and Virginia allow any district to borrow, but offer lower interest rates to districts with lower tax bases. Maine has a revolving renovation fund to encourage replacement of leased spaces with permanent structures. The state automatically forgives 30 to 70 percent of loans, depending on district wealth. Arkansas, Michigan, Mississippi , Montana, and Utah offer loans to all districts at the same interest rate.

Map 7: State Education Capital Loan Programs (2001)



Source: OEA, State School Construction Aid Survey

All 10 states with loan programs also have bond guarantee programs. Michigan has merged the two approaches in its School BondLoan Program. If a district is unable to pay bondholders, it may borrow from the program. However, districts levying above the state minimum may take out a loan regardless of the status of their bond issues.

Nonrecurring State Funding

Fourteen states passed some type of nonrecurring funding measure in the years 1996 to 2001.[20] (See Map 8.) Six of these (Alabama, California, Nevada, New Jersey, North Carolina, and South Carolina) represent state bond initiatives. The four largest state nonrecurring allocations per student were bond initiatives, including the $8.6 billion bond initiative for New Jersey's Facilities Construction and Renovation Program, a response to a court order. This program will provide $6,566 per student, though the amount spent in individual districts will vary greatly based on district wealth. The next largest per student allocation was North Carolina's 1996 bond initiative that raised an average of $1,427 per student. Districts with low property wealth and/or high enrollmentgrowth received higher funding.

[20] The office considered any funding not slated to occur on an annual basis in perpetuity to benonrecurring. In some cases, nonrecurring funding stretches over several years. Amounts given are totalnonrecurring allocations approved. In some cases, portions of this funding have not been distributed.

Map 8: Nonrecurring State Funding (1996-2001)

Source: OEA, State School Construction Aid Survey

Seven states have passed nonrecurring funding measures other than bond initiatives in the past five years:

Florida ($1,109 per student)—in 1997, the state legislature allocated $2.7 billion in lottery revenue for the next 20 years to fund the SMART Schools Act. The largest portion of this is Classrooms First ($2 billion). Districts may choose to receive this money as cash or bond proceeds but must use it to build new permanent classrooms. The remaining funds are allocated through six different programs. District funding through these programs is based on thrift, innovation, local effort, and rural location.

Georgia ($324 per student)—in 2001, the state legislature allocated $468 million to help districts meet state-mandated class size standards.

Idaho ($41 per student)—in 2000, the Idaho legislature established a $10 million revolving loan fund for school districts. However, the interest rate charged by the fund did not offer finance savings, so no district borrowed from the fund. In 2001, the legislature amended state statutes freeing this money to provide grants to local districts. The fund now helps districts pay interest on bonds and remedy unsafe or unhealthy conditions in schools.

Maryland ($12 per student)—in 2001, Maryland issued $9,828,000 in Qualified Zone Academy Bonds (QZABs).[21] Maryland issued QZABs for all eligible districts in the state, with the state paying principal costs normally borne by local school districts.

[21] QZABs are a federal program meant to help schools in high-poverty areas meet capital needs. School districts pay only the principal on QZABs. Buyers of QZABs receive a credit on their federal tax returns in lieu of interest

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New Hampshire ($266 per student)—New Hampshire has two nonrecurring programs. The first is a $9 million legislative allocation made in 2000 for vocational technology center renovations. The second is a seven-year $43 million matching grant of 75 percent to encourage local school districts to build kindergarten facilities. New Hampshire is the only state that does not require local districts to provide kindergarten.

New York ($66 per student)—the New York Legislature allocated $145 million for its RESCUE program for fiscal year 1999 and an additional $50 million for the following year. District grants were based on enrollment and could be used forseveral different purposes.

Wyoming ($223 per student)—the state legislature allocated $20 million in emergency funding in fiscal year 2001 to meet needs not covered by the state's Capital Construction program.

State Annual Funding Programs

Forty states including Tennessee have some type of annual funding program (See Map 9.) Many states have multiple programs or programs with multiple components. These programs are designed to give local school districts a reliable source of funding for ongoing capital needs.

Map 9: State Annual Funding Programs Spending (2001)

Source: OEA, School Construction Aid Survey

Of the 40 states with annual funding programs, only Arizona and Hawaii have established a state policy goal of meeting all capital needs of local districts exclusively with state

payments. State departments of education determine which schools in each state qualify to issue QZABs. All states received an allotment from which to issue QZABs.

funds. Thirty-two of the remaining 38 states allocate greater levels of funding to districts with lower tax bases. Florida, Vermont, and Maine do not directly increase aid to poorer districts, but do offer higher funding or priority to districts with greater needs, which can have the same effect. Indiana, New Hampshire, and Oregon do not fund capital outlay at higher levels in poorer districts. Thirteen states[22] offer some type of additional funding or priority to districts with higher rates of enrollment growth.

States also use a number of other methods to allocate annual aid. Several assess district needs at the state level to determine the amount of state funding available to each district. Others have specific funding sources for projects intended to remedy pressing health or safety issues. A few states also offer higher aid for consolidation projects or projects that use innovative solutions to reduce capital costs. Massachusetts provides higher levels of state aid to districts that maintain high maintenance ratings, hire project managers, and exceed energy efficiency standards. Finally, some states offer additional aid based on local effort. That is, districts that spend more (or tax at a higher level) receive more state aid than districts that choose not to spend as much.

Wisconsin's program of state aid to local districts differs considerably from other states. Operating expenses, capital outlay, and debt service all fall under the umbrella of shared costs in the state's equalization formula. No state funds are specifically earmarked for capital outlay. The state offers primary, secondary, and tertiary aid based on district spending per pupil. As districts spend more, they move from one category to the next, and each successive category offers a lower level of state matching funds. Several wealthy districts have guaranteed valuations above the amount set for tertiary aid. Each additional dollar these districts spend in the tertiary category results in *less* state aid from the secondary category. Thus, the Wisconsin funding formula has a disincentive for wealthier districts to spend significantly more than other districts.

State Oversight Mechanisms

As states take an increasingly prominent (and expensive) role in school capital finance, many have implemented procedures to ensure state funds are spent in accordance with state goals. Hawaii, Arizona, and Ohio have demonstrated the most significant state oversight. As with all education expenditures, Hawaii funds capital outlay at the state level; needs assessments and funding allocations are therefore somewhat isolated from local politics.

The Arizona legislature passed the Students FIRST program in 1998. Over 16 months, the state sent investigators to each of the state's 1,210 public school buildings to assess district needs. The School Facilities Board (SFB) estimated these needs will cost $1.1 billion ($1,290 per student), a total that will be covered entirely by state dollars drawn primarily from a 0.6 percent increase in the state sales tax. The SFB seeks local input, and liaisons from the SFB remain in contact with local districts. However, final decisions about what will be built rest with the state. The SFB contracts with construction agencies for projects, frequently bundling projects from multiple districts into a single bid in order to reduce construction costs.

[22] Alaska, Georgia, Hawaii, Kentucky, Maine, Maryland, Mississippi, New Jersey, New Mexico, New York, Texas, Vermont, Washington.

The Ohio legislature passed its Rebuilding Ohio Schools Program in 1997. The plan, like Arizona's, sent state assessors throughout the state todetermine each district's need. From this assessment, the state and districts construct Master Facilities Plans (MFPs). The state gives each district matching funds (based on property wealth)for projects contained in the MFP, and both the state School Facilities Commission and the State Controlling Board review projects.

Alternately, 15 states do not require districts to submit longrange facilities plans to the state and do not require the approval of any state body for district projects using state funds. Of this group, the only states with annual capital aid of more than $66 per student are Tennessee ($189) and Virginia ($171). Tennessee's capital outlay aid is a component of the state's BEP. Funding is based on average daily membership (ADM) and district fiscal capacity. However, districts are free to use capital outlay aid for other purposes and can use some other components of the BEP for capital outlay. Virginia distributes aid through a flat division grant, but also gives divisions aid based on average daily attendance (ADA), ADA growth, and division wealth (composite index).[23] Because Tennessee and Virginia base state aid on district wealth and size and not on specific projects, districts do not receive additional state funds by allowing facilities to fall into disrepair or by pursuing more elaborate projects despite the absence of formal state review.

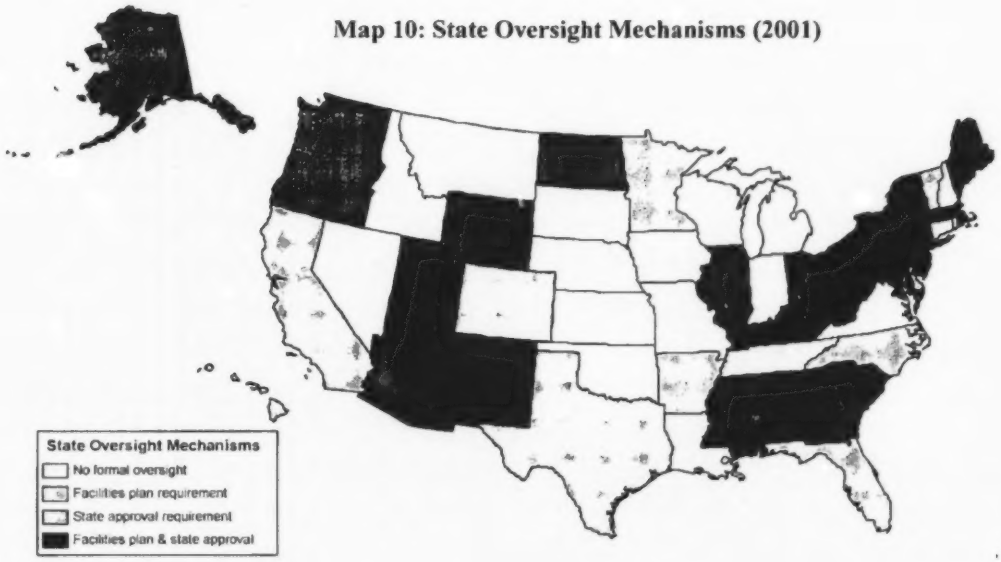
State Approval Bodies

Thirty-one states require a state-level body to review and approve individual local projects that use state funds. (See Map 10.) As state funding increases, districts have greater incentive to pursue more elaborate projects since they will bear smaller portions of their costs. The bodies that review these projects aremeant to ensure the projects are commensurate with district needs and are being completed in a costeffective manner. Twenty-five states require the state department of education (or its equivalent) and/or the state board of education to review projects. The remaining states, including Arizona and Ohio, have established boards with the specific purpose of overseeing K-12 capital outlay.

Most approval bodies generally fit within the above description, but there are nuances. For example, Kentucky has three major funding programs, only one of which mandates state project review. North Dakota has no capital funding program but requires state review for its loan program.

[23] Virginia's school divisions are roughly equivalent to school districts in other states.

Map 10: State Oversight Mechanisms (2001)



Source: OEA, School Construction Aid Survey

The establishment of approval bodies does not ensure state dollars will be used wisely. Review bodies with close ties to districts or elected officials or containing members who anticipate receiving funding in the near future for their districts, may view the applications with a bias or bend to pressure from districts. If this happens, review bodies lose much of their value as a check on the appropriateness of various expenditures. One survey respondent noted that some review bodies have avoided examination of less costly alternatives and included political considerations in a process that should be driven by needs.

Long-Range Facilities Plans

In 1999, 65 percent of public schools in the nation used long-range facilities plans.[24] Twenty-two states require all districts to submit long-range facilities plans to the state. Four additional states require districts to submit plans to receive state aid. (See Map 10.) These plans typically include an assessment of existing facilities capacity and the condition of those facilities in tandem with enrollment projections. States differ in the range of these plans, but the plans typically stretch 10 years. There is also great variance in how often plans must be revised and submitted to the state. The most common approach is to require districts to update their plans annually.

States usually use long-range facilities plans in conjunction with approval bodies. That is, those bodies utilize facilities plans submitted by districts in determining whether or not a project is necessary. Only four states that require districts to submit long-range plans do not review every state-funded project at the state level.

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[24] Bernie Green, project officer, *Condition of America's Public School Facilities: 1999*, (Washington, DC: National Center for Education Statistics, 2000), p. 29.

Federal Role in K-12 Capital Outlay and Debt Service

The federal government has traditionally played a limited role in K-12 education. The vast majority of public school capital funding still comes from state and local sources. However, because federal programs target funding to address specific problems they have had a significant impact on many districts in Tennessee and the nation as a whole.

Qualified Zone Academy Bonds

Congress created Qualified Zone Academy Bonds (QZABs) in 1997 to help schools with limited resources renovate or repair existing facilities. The federal government allotted $400 million in QZAB bonding authority for fiscal years 1998 through 2001, a total of $1.6 billion. Bonds authorized for FY01 must be issued by December 31, 2003. Each state received an allocation based on that state's populationbelow the federal poverty line.

State education agencies determine how to distribute QZABs.However, schools qualify for QZABs only if (1) they are located in an Enterprise Community or Empowerment Zone or (2) at least 35 percent of their students qualify for free or reduced-price school lunches. School districts pay only the principal on QZABs. Buyers of QZABs receive a credit on their federal tax returns in lieu of interest payments. Thus, QZABs offer significant finance savings to districts pursuing qualified capital projects. The federal government requires schools using QZABs to partner with businesses or other private entities. These groups must donate to the schools at least 10percent of the value of the money borrowed using the bonds. Acceptable donations include:

- Cash
- Goods, including equipment and technology
- Services, including help developing curriculum or using technology
- Internships or field trips that provide opportunities for students to learn outside a traditional classroom setting.[25]

Some qualifying rural districts in Tennessee have had difficulty meeting the 10 percent private donation requirement. Businesses generally choose to support schools in their communities. Because there are fewer businesses in rural communities, rural districts may find themselves unable to secure sufficient private donations to pursue major projects. Furthermore, securing private donations requires significant effort from local school districts, reducing the time school system officials can spend on their core duties.[26]

QZABs present other problems as well. Although federal law allows QZABs to be used for purposes other than capital projects (such as teacher training), the private acts governing most school districts do not allow them to incur debt for purposes other than capital projects. Also, despite offering essentially interest-free financing for these

[25] U.S. Department of Education, "Qualified Zone Academy Bonds—Technical Background," May 2, 2001, http://www.ed.gov/inits/construction/technicalqzab.html(accessed November 16, 2001).

[26] Interview with Mary Margaret Collier, Director of Bond Finance, Tennessee Office of the Comptoller, November 28, 2001.

projects, QZABs require local districts to pay the principal. This may be problematic for districts with low fiscal capacity. QZABs also require substantial coordination between school systems and local legislative bodies. Finally, many districts with pressing capital needs could meet these needs most effectively through new construction, but QZABs cannot be used for new construction projects.[27]

The IRS does not maintain records of other states' use of QZAB allocations.[28] Tennessee's total allocation for all four years is $33,077,000. The state issued $13,290,000 in QZABs on November 30, 1999 and issued $11,034,235 in December 2001 leaving $8,752,765 to issue by December 30, 2003.[29] In 2001, the General Assembly broadened the state's QZAB program to include qualified nonprofit corporations.[30] Project GRAD is a nonprofit corporation with significant involvement in the Knoxville area. The corporation has enlisted substantial private donors for its programs around the country and has no difficulty soliciting the 10 percent private match. Project GRAD will likely apply for any QZAB funds not claimed by districts by 2003 for projects in Knoxville. Thus, it is likely that Tennessee will use its entire QZAB allotment by the time the program expires.[31]

School Renovation, IDEA, and Technology Grants

The federal government authorized $1.2 billion for School Renovation, Individuals with Disabilities Act (IDEA), and Technology Grants to local districts in FY01. Of this, $901 million was given to states to distribute to local districts for urgent school repairs and renovations.[32] Tennessee received $17,371,541 ($13,028,656 for renovation) through this grant program. Districts with high poverty levels received priority for the grants.[33] On February 1, the department announced $10.6 million in Renovation Grants to local school districts from this funding. Individual grants ranged from $61,200 to $500,000.[34] Approximately $2.4 million in Renovation Grants were not distributed because the amount of federal funding earmarked for high poverty districts exceeded the grant requests submitted by those districts. The department is currently negotiating with the federal government to issue a second round of applications specifically for high poverty districts to use the remaining funds.[35] The department will distribute IDEA and Technology grants later this year.

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[27] Interview with Jim Jones, Director of Local School Finance, Tennessee Department of Education, November 27, 2001.

[28] Telephone interview with Timothy Jones, Assistant Branch Chief, U.S. Internal Revenue Service Tax-Exempt Bond Division, November 28, 2001.

[29] The 1999 issuance included projects for Kingsport City, Knox County, Lincoln County, Memphis City, Rhea County, Scott County, and Unicoi County Schools; the 2001 issuance included projects in Humboldt City, Montgomery County, and Memphis City Schools.

[30] TCA §48-101-301 (14)(C).

[31] Interview with Jim Jones, Director of Local School Finance, Tennessee Department of Education, November 27, 2001; Interview with Mary Margaret Collier, Director of Bond Finance, Tennessee Office of the Comptroller, November 28, 2001.

[32] U.S. Department of Education, "School Renovation, IDEA and Technology Grants Fact Sheet," May 25, 2001, http://www.ed.gov/inits/construction/rengrantshtml (accessed November 16, 2001).

[33] Tennessee Department of Education, "School Renovation, IDEA, and Technology Grants: Grant Process Description," November 6, 2001.

[34] Faye Taylor, "Weekly Message from the Commissioner," February 1, 2002.

[35] Phone interview with Jim Jones, Director of Local School Finance, Tennessee Department of Education, February 6, 2002.

State Infrastructure Banks

One potential federal program to address K-12 capital needs is state infrastructure banks. For the past two congressional sessions, Rep. Ellen Tauscher (D-CA) has introduced legislation to establish these banks. The banks would provide low-interest loans to schools or libraries pursuing capital projects. Rep. Tauscher's legislation would allocate $2.5 billion in federal funds over five years to provide the necessary start-up costs for the banks. The program would require states to match federal funds at 25 percent or more. After this initial infusion of federal and state funding, the banks should be self-sufficient as districts repay loans they take out.[36] The current version of Rep. Tauscher's (HR 1851) was referred to the House Subcommittee on Education Reform in July 2001 and has received no action since that time.[37]

Tennessee Capital Aid Programs

Basic Education Program

Tennessee funds K-12 education needs through its Basic Education Program (BEP). Within this funding mechanism are two broad divisions: classroom components and nonclassroom components. Based on district average daily membership (ADM), the BEP determines each district's basic need for personnel, textbooks, technology, capital expenses, and other categories. The state then funds 75 percent of the total BEP generated classroom needs and 50 percent of the total BEP generated nonclassroom needs for the state as a whole.

The amount of funding individual districts receive, however, varies with county fiscal capacity. The fiscal capacity index targets state revenue to those counties with less ability to raise revenue through property, sales, and other taxes and with greater needs for education spending based on the percent of the population in public schools. For the 2001-02 school year, the state portion of nonclassroom funding ranged from a low of 11.10 percent (Davidson County) to a high of 89.65 percent (Hancock County).[38]

BEP Capital Outlay Component

Nonclassroom components of the BEP include superintendents, system secretarial support, technology coordinators, school secretaries, maintenance and operations needs, non-instructional equipment, pupil transportation, staff benefits and insurance, and capital outlay. While the actual formula used by the BEP to determine capital funding is rather complicated, it can be broken down into three basic steps. First, the state calculates the system's need for school buildings based on enrollment using district ADM. The BEP then calculates the cost of those schools including construction, equipment, architects' fees, and financing. Finally, it divides that total cost by the expected 40-year life of a school building. This last number is the amount the BEP allocates for capital outlay for the district. The BEP allocated $363,418,429 for capital outlay for the 2001-02 school year. As part of the nonclassroom component of the BEP, the state funds half of the total

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[36] Thomas: Legislative Information on the Internet, "State Infrastructure Banks for Schools Act of 2001," http://thomas.loc.gov/cgi-bin/query/z?c107:H.R.185: (accessed November 16, 2001).
[37] Thomas: Legislative Information on the Internet, "Bill Summary and Status for the 107th Congress," http://thomas.loc.gov/cgi-bin/bdquery/z?d107:HR01851:@@@X (accessed July 24, 2002).
[38] Ibid.

capital outlay allocation, $181,709,215. This translates into approximately $202 per student.[39]

Capital outlay comprises approximately 35 percent of the nonclassroom portion of the BEP. It is important to note that school districts are not required to spend this money for school construction. The only stipulation on state BEP funding is that districts must spend money generated for classroom components on classroom activities and resources.[40] Thus, school districts could theoretically spend no money on construction and spend all state money from the capital outlay component in other areas, inside or outside the classroom. Conversely, school districts could spend the entirenonclassroom portion of state BEP funding on school construction.

Actual local education expenditures often exceed the BEPgenerated local share. In fiscal year 2000, Tennessee school districts spent a total of $611,091,742 for capital projects.[41] The BEP generated $329,404,480 in capital outlay funding for that year, 54 percent of actual spending. State BEP capital outlay funding was $164,702,240, only 27 percent of actual public K-12 capital spending.

BEP Growth Funding

Ordinarily, BEP funding is based on district ADM from the previous year. However, Tennessee state statute provides that if a school system's ADM changes from the prior year by more than two percent, the current year ADM will be used to generate BEP growth funding.[42] Growth funding only applies to additional ADM above two percent. For example, if a district with 1000 students grew by 40 students (four percent) in one year, the district would receive additional funding for 20 of those students. Growth funding for these students would equal the state BEP funding per pupil.The General Assembly appropriated $10.5 million in 2000-01 to fund ADM growth above two percent. This funding lies outside the BEP formula. Districts exercise a high degree of local control over how they spend growth funding. However, they must spend at least the same percentage of growth funding on classroom needs as the BEP allocates the district for classroom expenses. Forty-one districts received growth funding inthe 2000-01 school year. District aid averaged $256,098.

Growth funding is not designed to providehigh-growth districts with greater funding than those with stable populations. Instead, it provides funding that takes into account enrollment growth. All things being equal, the BEP generates more funding per pupil for a district with stable enrollment than both BEP and growth funding for a district with enrollment growth. Without growth funding, districts withhigh rates of growth would receive significantly less state funding per pupil.

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[39] 2002 BEP Model, Tennessee Department of Education.
[40] TCA §49-3-354(b).
[41] Tennessee Department of Education,*Annual Financial Report for the Scholastic Year ending June 30, 2000.*
[42] TCA §49-3-351(d). If additional funds are available, districts with growth of less than two percent may receive growth funding. In fiscal year 2002, only districts with at least two percent received funding.

Other programs

Tennessee channels all annual state capital funding through the BEP. It does not have a credit enhancement program or a fund to provide loans to districts.The state has not provided any nonrecurring capital funding to districts in recent history.

Tennessee Capital Aid Spending

Using data from the State School Construction Aid Survey OEA staff calculated state spending totals by dividing all nonrecurring spending from the past five years by five (to get an annual nonrecurring estimate) and adding that number to 2000-01 spending under each state's annual capital funding program. This sum was then divided by 2000-01 estimated membership to reveal total annual spending per pupil.[43] Obviously, this number is a rough estimate that could be influenced in either direction by any of the following criteria:

- A general predisposition in the state away from state spending toward local spending or vice versa.
- A general predisposition in state education funding away from state spending toward local spending or vice versa.
- A state education funding apparatus that gives local districts more responsibility for operating expenses while the state pays more for capital outlay or vice versa.
- Significant nonrecurring state capital outlay spending prior to the period covered in this study (1980s or early 1990s) or the absence of state spending during that time.
- Significant changes in annual state spending in the years leading up to 2000-01.

Any judgments about a specific state's capital funding programs should be made in light of these qualifications and should account for state characteristics that would not be expressed by these estimates. Based on this methodology, Tennessee spends slightly less on capital outlay than the national average and the average among its border states (See Chart 1.) Seven states that have not spent any state money on K-12 capital funding programs over the past five years drive the national average down from $282per student to $248 per student.

[43] Wisconsin's funding system is unique in placing capital outlay and debt service within the larger rubric of shared costs. No component of shared costs is computed individually, and the size of the state match depends on actual district spending. These features make it impossible to isolate state funding targeted for capitaloutlay and debt service. Because of this, Wisconsin was not included in any funding calculations.

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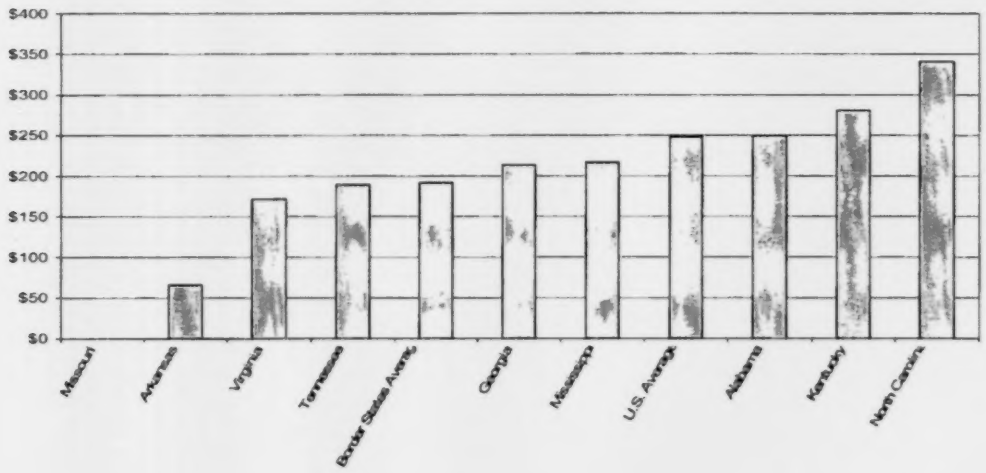
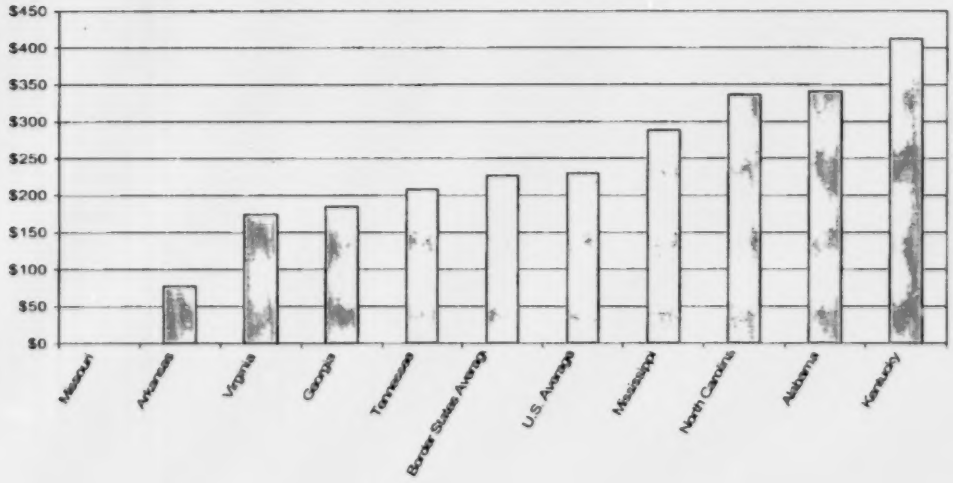
Chart 1: State Capital Spending Per Pupil



Though most criteria that may influence state capital spending data are difficult (if not impossible) to quantify, one remaining factor influencing state expenditures is quantifiable—membership growth. School districts must spend considerably more to build additional schools for new students than to maintain and replace schools for existing students. Because of this, the office adjusted these spending levels to account for enrollment growth (See Chart 2; see Appendix C for methodology.)

Chart 2: Growth-Adjusted State Capital Spending Per Pupil



According to this data, Tennessee spends 77 percent of the national average state K-12 capital spending per pupil. When adjusted for enrollment growth, Tennessee spends 90 percent of the national average.

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Analysis and Conclusions

Based on the condition of existing facilities, Tennessee's school construction needs are significant but less than those found in other states. In January 2002, the Tennessee Advisory Commission on Intergovernmental Relations (TACIR) released its Draft Commission Report on the Tennessee Public Infrastructure Needs Inventory.The inventory is a compilation of information submitted by local officials. Based on these responses, 74 percent of Tennessee's public schools were in "good" or "excellent" condition in July 2001.[44] Still, local officials reported approximately $3.34 billion in education capital needs over the 5-year period of the study (July 2001 through June 2006).[45]

In the 1996 GAO study, *School Facilities: America's Schools Report Differing Conditions*, 74.7 percent of Tennessee's K-12 schools required some improvement to bring them into good overall condition. While that number seems high, only four states had a lower percentage of schools requiring improvements.[46] The nationwide average cost to bring a school to good overall condition was $1.7 million. In Tennessee, only 12.5 percent of schools required more than $1.7 million in improvements to reach good condition. Thirty-nine states had a higher percentage of schools requiring major improvements.[47] Because the GAO study was based on survey data, it did not provide estimates of the total state need for repair and replacement of schools. As other states have made major efforts over the past five years to improve the condition of school facilities, it is possible that Tennessee's relative position has fallen somewhat. Still, based on current conditions of school facilities, it is likely that Tennessee's school construction needs are slightly lower than the rest of the nation.

Based on enrollment growth, Tennessee's school construction needs are comparable to those of the rest of the nation and will decline in the coming decade. Tennessee's birth rate and immigration rate were both below the national averages during the 1990s, but the state experienced an estimated net migration of 356,907 people from other states during that time.[48] These factors combined to produce public school enrollment growth slightly below the national average over the past decade. (SeeTable 1.) Tennessee's birth rate is expected to drop significantly over the coming decade, but NCES predicts its enrollment growth rate to remain above the national average. NCES pojects Tennessee's public K-12 enrollment will grow by 1.7 percent from 2000 to 2009.[49] (See Table 1.) However, growth rates for individual districts will vary considerably. From 1992 to 2001 average daily membership declined by 34 percent (3.0 percent annually) in Fayette County while ADM increased by 62 percent (5.5 percent annually) in Williamson County over the same period[50]

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[44] Tennessee Advisory Commission on Intergovernmental Relations, "Draft Commission Report on the Tennessee Public Infrastructure Needs Inventory," January 28, 2002, p. 27.
[45] Ibid., p. 26.
[46] Hawaii, Montana, Pennsylvania and Georgia.
[47] US General Accounting Office,, "School Facilities: America's Schools Report Differing Conditions," June 1996.
[48] US Census Bureau, "State Population Estimates and Demographic Components of Population Change: April 1, 1990 to July 1, 1999," December 29, 1999.
[49] National Center for Education Statistics, *Projections of Education Statistics to 2011*, August 2001, Table 4.
[50] Office of Education Accountability, internal review and analysis of school system data

Table 1: K-12 Enrollment Growth

	1991-2000	2000-2009
Tennessee	9.8%	1.7%
U.S.	10.6%	0.3%

Sources: National Center for Education Statistics, *Projections of Education Statistics to 2009*, July 1999, and National Center for Education Statistics, *Projections of Education Statistics to 2011*, August 2001.

Legal challenges have increased state capital funding in Tennessee, but not to the extent found in other states. Tennessee's BEP funding, including the capital outlay component, is a response to a lawsuit brought against the state. In *Small Schools v. McWherter*, the Tennessee Supreme Court ruled that the state's existing funding methods did not provide equitable funding to children in rural areas. In anticipation of the court's 1993 decision, the General Assembly implemented the BEP through the 1992 Education Improvement Act to address these issues. Plaintiffs challenged the adequacy of some aspects of BEP funding, including capital outlay, in *Small Schools v. McWherter II*. However, the court ruled in favor of the state on the issue of capital, and the original school construction component of the BEP has remained intact.

The impact of legal challenges on capital funding has varied across the states; the scope of *Small Schools v. McWherter* falls in the middle of this range. Many states have faced court decisions with much broader implications. Arizona, for example, initiated its Students FIRST program in 1998 in response to the state supreme court's *Roosevelt Elementary School District No. 66 v. Bishop* decision. The state passed a 0.6 percent sales tax to fund this program, which seeks to meet all capital needs faced by every district with state funding. In contrast, some states with less extensive capital funding than Tennessee have successfully defeated legal challenges to their programs.

Tennessee school districts must construct new facilities to remain in compliance with EIA class size mandates. The Education Improvement Act (EIA) passed by the General Assembly in 1992 established strict limits on class size throughout the state.[51] These limits created the need not only for more teachers but also for additional classrooms. TACIR's infrastructure report cited a cost of $1.35 billion for construction of new classrooms from July 2001 to June 2006 in order to house classes mandated by the EIA.[52] Assuming school districts finance these costs over a number of years, annual costs for EIA-driven classrooms will be considerably lower. TACIR based its estimate on student/teacher ratios for the 1991-92 and 2000-01 school years and enrollment growth patterns.

[51] TCA §49-1-104.

[52] Tennessee Advisory Commission on Intergovernmental Relations, "Draft Commission Report on the Tennessee Public Infrastructure Needs Inventory," January 28, 2002, p. 28.

Total K-12 capital spending in Tennessee increased rapidly over the past decade. In constant 1997 dollars, total public K-12 capital spending[53] in Tennessee grew from $185,879,267 in 1990 to $380,039,655 in 1997. This represents an increase of 104.5 percent in only seven years even after adjusting for inflation, compared to 39 percent nationwide.[54] Average daily membership (ADM) grew 8.2 percent during this time. Inflation-adjusted spending per ADM increased 89 percent from 1990 to1997, reaching $426.[55] While capital spending in Tennessee rose much more rapidly in the 1990s than in the nation as a whole, in 1997 it remained approximately 20 percent below the national average of $535 per pupil.[56] This variance is probably partially due to lower construction costs. RS Means estimated that commercial construction costs in Tennessee ranged from 68 percent to 86 percent of the national averagein 2000.[57]

Recent national data that correlates to the 1997 GAO report is unavailable. However, school district spending on capital projects in Tennessee has continued to grow rapidly. According to the Tennessee Department of Education Annual Financial Reports, K-12 capital spending, when adjusted for inflation,[58] increased by 75 percent from fiscal year 1997 to fiscal year 2001.[59]

High levels of local spending in recent years have improved the conditions of Tennessee's schools. TACIR's Public Infrastructure Needs Inventory for July 2001 through June 2006 found that 74 percent of Tennessee's schools were in good or excellent condition.[60] This is an increase from 69 percent in the previous report, covering July 1999 to June 2004.[61] The report also found a cost of $1.35 billion to comply with EIA class size mandates, a decrease from $1.63 billion in the previous report.[62] These findings indicate Tennessee is making progress in addressing facilities needs.

Improvements in the conditions of school facilities are largely the result of local spending. In fiscal year 2001, Tennessee school districts spent $743,051,026 on capital projects.[63] The BEP capital outlay component generated $342,836,862 for that year (46 percent of total capital spending). Since the state funds half of the BEP capital outlay

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[53] Local capital spending including local revenue, state funding, and national funding.
[54] US General Accounting Office, "School Facilities: Construction Expenditures Have Grown Significantly in Recent Years," March 2000, p. 27.
[55] Tennessee Department of Education,*Annual Statistical Report for the Scholastic Year ending June 30, 1990*, Table 7A and Tennessee Department of Education,*Annual Statistical Report for the Scholastic Year ending June 30, 1997*, Table 7A.
[56] Based on NCES enrollment data. National Center for Education Statistics,*Projections of Education Statistics to 2011*, August 2001, p. 27.
[57] RS Means, *Square Foot Costs, 22nd Annual Edition*, ed. Barbara Balboni, 2001, p. 434.
[58] Using Engineering News Record "Construction Cost Index,"http://www.enr.com/cost/costcci.asp(accessed January 22, 2002).
[59] Tennessee Department of Education,*Annual Financial Report for the Scholastic Year ending June 30, 2001*, Budget Codes 76100000 and 91300000 and Tennessee Department of Education,*Annual Financial Report for the Scholastic Year ending June 30, 1997*, Budget Codes 76100000 and 91300000.
[60] Tennessee Advisory Commission on Intergovernmental Relations, "Draft Commission Report on the Tennessee Public Infrastructure Needs Inventory," January 28, 2002, p. 27.
[61] Tennessee Advisory Commission on Intergovernmental Relations,*Building Tennessee's Tomorrow: A Survey of Infrastructure Needs*, February 2001, p. 28.
[62] TACIR 2002, p. 28 and TACIR 2001, p. 30.
[63] Tennessee Department of Education,*Annual Financial Report for the Scholastic Year ending June 30, 2001*, budget codes 76100000 and 91300000.

component, state spending for fiscal year 2001 was $171,918,431. Thus, state funding comprised only 23 percent of Tennessee K-12 capital spending in 2001.

Tennessee lacks consistent and clear data on district-level capital projects and spending. As part of the Education Improvement Act of 1992, over 3,700 State Board rules and regulations were purged in order to promote LEA flexibility. Several eliminated rules dealt with reporting and monitoring of school construction and facilities.[64] The Department of Education and the Comptroller's Division of Local Finance bothmaintain substantial financial data on capital spending and bonded debt, but it is not easily analyzable. The Department's Annual Financial Reports contain budget codes for capital spending but do not show the number, cost, and type of individual projects.The Division of Local Finance maintains records of bond issues for K-12 capital projects within a larger database of local government debt. In order to examine school district debt in isolation, these bond issuances must be pulled from the database manually.

Though Tennessee spends below the national average for K-12 construction and renovation projects, the state spending for capital outlay is high relative to other state programs. Because Tennessee is a low-spending state, K-12 capital outlay receives *more* funding relative to other programs while still being funded at lower levelsthan other states. In fiscal year 2001, the BEP's capital outlay component generated $189 in state funding per pupil, though it is important to note the state does notearmark those funds for capital outlay. The same year, Tennessee spent an estimated $3,328 state dollars per pupil on K-12 education. This amount is 68 percent of the national average.[65] Thus, Tennessee's state government spends relatively more on capital outlay than it does on other facets of education spending. Based on data from the U.S. Census Bureau and the U.S. Bureau of Economic Analysis, Tennessee's per capita tax burden for the year 2000 was $1,360. This is only 71 percent of the national average of $1,921 per capita,[66] indicating that Tennessee spends relatively more on K-12 capital outlay than it does on government services taken as a whole.(See Table 2.)

[64] Correspondence from Faye Taylor, Tennessee Commissioner of Education, July 19, 2002.
[65] "Estimated Fiscal 2001 Elementary and Secondary Education Expenditures," National Association of State Budget Officers, *2000 State Expenditure Report*, June 2001, p. 17; National Center for Education Statistics, *Projections of Education Statistics to 2011*, August 2001, Table 4.
[66] Federation of Tax Administrators, "2000 State Tax Revenue," http://www.taxadmin.org/fta/rate/00taxbur.html (accessed November 7, 2001).

Table 2: Tennessee Spending Compared to National Averages

	Tennessee	National Average	Percent of National Average
State K-12 Capital Spending per Pupil	$189	$248	77%
State K-12 Total Spending per Pupil	$3,328	$4,859	68%
State Tax Revenue per Capita	$1,360	$1,921	71%

Sources:
K-12 Capital Spending per Pupil: OEA State School Construction Aid Survey
K-12 Total Spending per Pupil: "Estimated Fiscal 2001 Elementary and Secondary Education Expenditures," National Association of State Budget Officers, *2000 State Expenditure Report*, June 2001, p. 17; National Center for Education Statistics, *Projections of Education Statistics to 2011*, August 2001, Table 4.
State Tax Revenue per Capita: Federation of Tax Administrators, "2000 State Tax Revenue," http://www.taxadmin.org/fta/rate/00taxbur.html (accessed November 7, 2001).

Tennessee's methods of BEP funding provide districts with high levels of local control. Tennessee does not require local districts to submit longrange facilities plans to the state, nor does it require state approval for capital projects using state BEP funding. Thus, school district officials are free to meet local needs in the manner they believe most effective without altering their projects or goals to meet state standards. State oversight mechanisms could ensure that capital projects advance state priorities, but such mechanisms would probably lengthen project completion time and consume additional state and local resources.

Tennessee also demonstrates a high degree of local control in allowing districts to use BEP-generated dollars for a number of purposes. Districts may use funds generated by the BEP capital outlay component to meet other needs. Also, certain other components of the BEP may be used for capital outlay and debt service, and districts are free to spend more or less than their local portion of BEP school construction funding would indicate. These features give local districts significant latitude with which to allocate state resources. Because of this emphasis on local control, the department does not maintain staff dedicated to capital outlay.

Strengths of Tennessee's Current Funding Program

BEP funding is stable. The BEP formula creates a consistent funding source for local districts. Local districts can generally anticipate state funding to remain constant or to increase each year.[67] If the local tax base shrinks, state funding will increase through the fiscal capacity index. If the district experiences rapid growth, it receives BEP growth factor funding. These features allow local districts to plan to meet current and future needs based on a stable combination of state and local revenue.

Tennessee provides higher levels of capital funding to districts with limited local revenues. Tennessee funds half of the total nonclassroom BEP-generated funding needs, including capital outlay. However, the amount of state funding each district receives

[67] State BEP funding could decrease if (1) a district's ADM declines or (2) a district's fiscal capacity increases.

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varies considerably depending on county capacity. This mechanism enhances the ability of districts with smaller tax bases to pursue capital projects.

The structure of the BEP does not allow districts to artificially increase their level of state capital funding. Generally, states that provide substantial capital funding to local districts do so on a project basis. That is, districts submit requests for state aid for individual projects to the state, and the state approves, modifies, or rejects these requests. In these scenarios, districts have an incentive to pursue more elaborate and costly projects since they will receive greater state funding if they do so. This market dynamic has the potential to increase state capital aid payments dramatically.

Instead of funding individual projects, Tennessee provides BEP funding for capital needs based on underlying needs for state capital aid: enrollment and fiscal capacity. The number and cost of capital projects that districts pursue does not affect the level of state funding districts receive. If districts choose to pursue more elaborate projects, they must bear all additional costs.

The structure of BEP funding provides implicit incentives for cost-effectiveness. Some states offer increased state aid to districts that seek to increase cost effectiveness. In these states, districts that use innovative solutions to reduce capital costs, maintain high maintenance ratings, hire project managers, or exceed energy efficiency standards may qualify for greater funding. Though the BEP does not provide any such explicit incentives to encourage districts to make cost-effective decisions, it does contain strong implicit incentives. State law requires districts to spend the BEP-generated local share, but districts do not receive more state funding for local spending beyond this level.

Every district in Tennessee spends more than its BEP-generated local share.[68] This implies that districts pursue an optimal funding level higher than that set by the BEP. This may mean that state funding is too low and districts must spend large amounts of local revenue to meet needs. The positive result is that lower levels of state funding encourage districts to behave in a cost-effective manner. For example, districts have an incentive to maintain buildings properly to reduce future local capital expenditures. They may also choose not to include less necessary features in new schools because they must pay the additional cost of these features using only local revenue.

Weaknesses of Tennessee's Current Funding Program

The BEP capital outlay component does not adjust for rapid enrollment growth. It is significantly more expensive to build schools for new students than it is to maintain and replace school buildings over time for a stable student body. The BEP growth factor attempts to provide districts with funding commensurate with actual enrollments for the current year when those enrollments are more than two percent above the previous year. However, it does not provide these districts any additional funding to address their need for increased capital spending. Because of rapid enrollment growth over the past decade, many Tennessee districts have been forced to spend substantial local revenue to meet capital needs.

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[68] Office of Education Accountability, internal review and analysis of school system data

Some districts may have difficulty raising additional local revenue to meet needs not funded by the BEP. Districts must use local revenue sources alone to cover any expenses beyond what is coveredby the BEP. In districts where a large percentage of the voting population has no ties to the public schools,voters and local legislative bodies may refuse to fund these expenses. Districts also may lack the property and sales tax bases necessary to raise significant local revenues. Some schools could have unmet needs because of an inability to secure local funding above the BEP.

The BEP does not include a mechanism to reduce borrowing costs. School districts in Tennessee primarily finance school construction throughtax-exempt general obligation bonds. Though bondholders do not have to pay taxes on the earnings o these bonds (allowing districts to offer lower rates of return on them than on corporate bonds), finance costs still account for roughly half of the costs of building a new school. Almost all districts in Tennessee purchase credit enhancement from private groups in order to lower borrowing costs. Tennessee is one of 19 stateswithout a credit enhancement program, state loan program, or other method of reducing district borrowing costs.

Recommendations

The General Assembly may wish to consider implementing a credit enhancement program to lower finance costs facing local school districts. Credit enhancement programs can offer local districts significant finance savings. State governments that implement such programs usually bear only the relatively small costs necessary to administer the programs. Twenty-nine other states have some type of credit enhancement program.

The General Assembly may wish to increase BEP capital outlay funding within the context of increases in overall BEP spending. School districts clearly spend significantly more on capital outlay expenses than the BEP generates. In the 2000-01 school year, state BEP capital funding was only 23 percent of actual expenditures on K-12 capital projects. Existing research suggests a link between the condition of school facilities and student performance. However, other research has shown strong links between spending in other areas and student performance, suggesting capital funding increases should be balanced against the need for more direct academic expenditures.

The General Assembly may wish to consider incorporating an additional factor within the BEP capital outlay component to account for rapid enrollment growth. Districts with high levels of enrollment growth must spend more on capital outlay than districts with stable student populations. Currently, districts must meet the additional marginal capital expenses of enrollment growth with only local funds. BEP funding targeted toward high-growth districts would better enable them to meet their greater capital needs.

Appendix A: State School Construction Aid Survey

(July 30, 2001)

State: _____

Name of Respondent: _____

Agency: _____

Title: _____

Phone #: _____

E-mail address: _____

1. What was the total K-12 enrollment of your state for 2000-01? _____
2. What is the approximate breakdown of funding for public school construction in the percent from federal/state/local/other sources?

   Federal _____% Local _____%

   State _____% Other _____%

3. Check the methods your state uses to assist school districts in new school construction and check if the state targets those methods toward districts with low wealth and/or high enrollment growth.

		Low Wealth	High Growth
_____	state guarantee of local bonds	_____	_____
_____	low-interest loans	_____	_____
_____	annual direct financial aid	_____	_____
_____	state-issued bonds (non-annual)	_____	_____

4. Does your state guarantee county and municipal bonds dedicated to school construction? Yes No

   If yes, what are the state's requirements for this program and what is the nature of the guarantee?

   _____

   _____

   _____

   _____

   _____

5. Does your state offer low-interest loans to local governments for school construction? Yes No

If yes, what are the state's requirements for these loans?

_____

_____

_____

_____

If yes, what is the total level of funds available for these loans? _____

How much can each individual district borrow at any given time? _____

_____

_____

_____

6. Does your state require districts to submit a long-range facilities plan to the state? Yes No

7. a. Does your state allocate money on an annual basis that is dedicated to school construction or to reimbursing local districts for school construction expenditures? Yes No

b. How much was the total annual appropriation for 1998 -99? $_____

c. For 1999-2000? $_____

d. For 2000-01, please list allocation by revenue source.

General fund	$_____
Education fund	$_____
Tobacco settlement money	$_____
State lottery	$_____
Trust fund	$_____
Other _____	$_____
Other _____	$_____
Total 2000-01 allocation	$_____

8. In the past 5 years, has your state implemented any one -time allocations of state money for school construction? (For example, has your state passed any new bond measures?) Yes No

   If yes, list the year, type, and amount of these allocations individually.

   Year Type Amount

   _____

   _____

9. What mechanism does your state use to allocate school construction funds to local districts? If your state uses a combination of mechanisms, please check each and give the percent of total direct aid governed by each criteria.

		Weight
_____	first come, first served basis	_____%
_____	local spending level (state match)	_____%
_____	property tax base	_____%
_____	sales tax base	_____%
_____	local tax revenue	_____%
_____	enrollment	_____%
_____	attendance	_____%
_____	enrollment growth	_____%
_____	school space per student	_____%
_____	age of buildings	_____%
_____	state determination of need through review process	_____%
_____	district bonded indebtedness	_____%
_____	other _____	_____%
_____	other _____	_____%

Please provide any other information you think relevant on how your state allocates school construction funds. _____

_____

_____

10. Does your state require a state body or agency to approve school construction proposals that use state money? Yes No

If yes, please list the bodies and circle whether they are within the state's executive (E) or legislative (L) branch.

Body	Branch
_____	E L
_____	E L

11. Does your state have any additional methods of financing school construction or renovation? Yes No

If yes, what are these methods and what is their scope?

_____

_____

_____

_____

_____

_____

_____

12. a. Is any part of your state's school capital funding program a response to a lawsuit? Yes No

If yes, please give the name of the lawsuit and the year filed. _____

_____

b. Are any lawsuits currently pending relating to your state's school capital funding program? Yes No

If yes, please give the name of the lawsuit and the year filed. _____

_____

Please return this survey to Richard Gurley, Legislative Research Analyst:

By mail: Richard Gurley
Offices of Research and Education Accountability
505 Deaderick St., Suite 500
Nashville, TN 37243-0268

By e-mail: rgurley@mail.state.tn.us

Or by fax: (615) 532-9237

If you feel any of the above questions require a more detailed explanation than can be given in the available space, please elabor ate on additional pages or clarify by phone or e -mail. Call or e-mail Richard Gurley with any questions at (615) 532 -1111 ext. 508 or rgurley@mail.state.tn.us . Thank you for your time and participation.

Appendix B: Additional Outside Resources

Education Commission of the States, "Recent State Legislation: Finance —Facilities," (Available online at http://www.ecs.org/html/offsite.asp?document=%2Fecs%2Fecscat%2Ensf%2FWebTopicView%3FOpenView%26RestrictToCategory%3DFinance%2D%2DFacilities)

Education Commission of the States, "School Finance Litigation," M arch 2000. (Available online at http://www.ecs.org/clearinghouse/18/23/1823.pdf)

Education Week, "Building A New Role: States and School Facilities," June 2001. (Available online at http://www.edweek.org/sreports/construction.htm)

Gardner, Nancy, "Key Aspects of State School Capital Financing," National Conference of State Legislatures, 18 September 2001.

Moody's Rating Methodology *Public Finance Handbook*, Moody's Investors Services, NY 2000, p. 111-124.

National Center for Education Statistics, "Public School Finance Programs of the United States and Canada: 1998-99." (Available online at http://nces.ed.gov/edfin/state_finance/StateFinancing.asp)

National Center for Education Statistics, "Early Estimates of Public Elementary and Secondary Education Statistics: School Year 2000-2001," Lena McDowell, February 2001. (Available online at http://nces.ed.gov/pubs2001/2001331.pdf)

National Governors Association, Education Policy Studies Div ision, "Building America's Schools: State Efforts to Address School Facility Needs," 14 June 2000. (Available online at http://www.nga.org/center/divisions/1,1188,C_ISSUE_BRIEF^D_384,00.html)

Shull, Laurel. "Update of School Construction Assistance Programs Study," MGT of America, 18 September 2001.

Standard and Poor's *Public Finance Criteria 2000*, McGraw-Hill, NY 2000, p. 57-73.

Appendix C: Enrollment Growth Funding Adjustment Methodology

The office regressed 1990-91 membership and ten-year absolute membership growth against previously calculated Total Annual Spending numbers. The intercept for this regression was 21,410,431 ($p=0.71$) and the coefficients were 152 for 1990-91 membership ($p=0.13$) and 777 for ten-year membership growth ($p=0.06$). From a base of $21 million, states spend an average of $152 additional dollars for each student in public school in 1990 and $777 for each net additional student who enrolled in public school during the following ten years. Thus, states spend about five times as much on new students obtained over a ten-year period as they do on existing students. This makes sense intuitively. If we assume school buildings have a fifty-year life, spending tied to growth over a ten-year period should have a five-to-one relationship to spending tied to existing enrollment. Building a new 200-student elementary school for new students costs the same as periodically replacing one of five 200-student elementary schools for 1000 existing students every ten years.

The office placed actual membership numbers for each state in the regression formula to derive a target growth-adjusted spending total for every state, which was divided by 2000-01 membership to achieve a growth-adjusted per pupil spending target. This number was then divided by previously calculated total annual spending per pupil numbers and multiplied by the weighted national average ($254.04) in order to determine growth-adjusted spending per pupil. Again, this should not be viewed as a concrete determination of the level of state funding but as the best possible estimate using data from this data set.

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